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FOLLOWING OECD PARIS SENT ACTION SECSTATE INFO ATHENS APR 8;
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SUBJECT: ECONOMIC AND DEVELOPMENT REVIEW COMMITTEE (EDRC)

REVIEW OF GREECE, APRIL 14, 1976

REF: EDR(76)8

1. SUMMARY: IN REFDOC CIRCULATED FOR APRIL 14 EDRC
REVIEW OF GREECE, SECRETARIAT ESTIMATES THAT REAL GREEK
GDP GREW BY 3.5 PERCENT IN 1975, A PERFORMANCE WHICH
EXCEEDED EVEN OFFICIAL EXPECTATIONS AND WHICH WAS
SUPPORTED BY EXPANSIONARY MONETARY AND FISCAL POLICIES
AND BY INCREASE OF RESIDENTIAL INVESTMENT AND PRIVATE
CONSUMPTION. WAGE AND PRICE INCREASES IN 1975 WERE SUB-
STANTIAL (ALTHOUGH MODERATE COMPARED TO 1974), AND LABOR
MARKET REMAINED WEAK. CURRENT ACCOUNT DEFICIT DECLINED
TO \$1 BILLION IN 1975 FROM \$1.2 BILLION IN 1974. FOR
1976, GREEK AUTHORITIES PROJECT 4 PERCENT INCREASE IN
GNP, 10 PERCENT INCREASE IN CONSUMER PRICES, AND CURRENT
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ACCOUNT DEFICIT OF \$1 BILLION. SECRETARIAT FEELS THAT
GROWTH ESTIMATE IS ON LOW SIDE, THAT PRICE PROJECTION IS
BARELY ACHIEVABLE AND THAT CURRENT ACCOUNT DEFICIT WILL
WIDEN TO \$1.2 BILLION. THUS, SECRETARIAT CONCLUDES

THAT EXPANSIONARY FISCAL POLICY PLANNED BY GREEKS FOR 1976 IS AT MAXIMUM LIMIT OF PRUDENCE. FOR MEDIUM TERM, SECRETARIAT SEES NEED FOR GREEKS TO (A) NARROW CONSIDERABLY THE CURRENT ACCOUNT DEFICIT, (B) GENERATE SIGNIFICANT INCREASE IN COMMODITY EXPORTS, SINCE SECRETARIAT SEES SLOW GROWTH IN INVISIBLE EARNINGS; (C) INCREASE SHARE OF MANUFACTURING INVESTMENT IN TOTAL INVESTMENT SPENDING; (D) IMPLEMENTATION OF EFFECTIVE INCOMES POLICY TO SUPPORT ALL OF ABOVE. ACTION REQUESTED: MISSION WOULD APPRECIATE COMMENTS/QUESTIONS WHICH COULD BE USEFULLY POSED AT EDRC REVIEW. FOR ATHENS: MISSION WOULD WELCOME COMMENTS ON SECRETARIAT ANALYSIS AND CONCLUSIONS AS WELL AS PARTICIPATION IN REVIEW BY EMBASSY REPRESENTATIVE. END SUMMARY.

2. SHORT-TERM OUTLOOK; DOMESTIC PROSPECTS: SECRETARIAT NOTES THAT IN 1975 GREEK REAL GDP GREW BY 3.5 PERCENT IN SPITE OF OECD-AREA RECESSION - A PERFORMANCE WHICH EXCEEDED EVEN OFFICIAL FORECASTS. GROWTH WAS PRIMARILY ATTRIBUTABLE TO EXPANSIONARY MONETARY AND FISCAL POLICIES, INCREASE IN RESIDENTIAL CONSTRUCTION AND STRONG GROWTH IN PRIVATE CONSUMPTION. PARTICULARLY NOTEWORTHY WAS COUNTER-CYCLICAL BEHAVIOR OF SAVINGS RATE WHICH, AFTER LARGE DROP IN 1974, STABILIZED AT LOW LEVEL IN 1975, THUS ALLOWING DEMAND MANAGEMENT POLICIES TO HAVE MAXIMUM IMPACT.

3. WAGE AND PRICE DEVELOPMENTS IN 1975 WERE LESS FAVORABLE, WITH WAGES AND SALARIES INCREASING BY 16-17.5 PERCENT (AND UNIT LABOR COSTS BY 10 PERCENT), AND CONSUMER PRICES 13.7 PERCENT OVER 1974 AVERAGE. MOREOVER, SECRETARIAT NOTES THAT GNP GROWTH IN 1975 WAS INSUFFICIENT TO GENERATE SIGNIFICANT INCREASE IN EMPLOYMENT, AND THAT RETURN OF WORKERS FROM ABROAD AND INCREASE IN DOMESTIC LABOR SUPPLY INDICATE THAT UNEMPLOYMENT INCREASED SUBSTANTIALLY DURING THE YEAR.

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4. FOR 1976, SECRETARIAT FEELS THAT OFFICIALLY PROJECTED 4 PERCENT GROWTH IN GNP IS EASILY ATTAINABLE AND THAT OUTCOME IS MORE LIKELY TO BE IN 4.5-5 PERCENT RANGE, WITH MAIN FORCES OF EXPANSION BEING PUBLIC AND PRIVATE CONSUMPTION AND RESIDENTIAL CONSTRUCTION. (SECRETARIAT POINTS WITH CONCERN TO EXPECTED STAGNATION OF BUSINESS FIXED INVESTMENT IN 1976.) NEVERTHELESS, SECRETARIAT NOTES THAT A GROWTH RATE OF THIS ORDER WOULD GENERATE ONLY SMALL INCREASE IN EMPLOYMENT AND THAT UNEMPLOYMENT MIGHT RISE FURTHER, PARTICULARLY IF THERE IS A CONTINUING NET RETURN OF WORKERS FROM ABROAD. GREEKS PROJECT 10 PERCENT INCREASE IN PRICES IN 1976.

SECRETARIAT NOTES THAT EFFECTS OF IMPORTANT INFLATIONARY FACTORS IN 1975 - DRACHMA DEPRECIATION AND INDIRECT TAX INCREASE - HAVE WORKED THROUGH, SO THAT SOME IMPROVEMENT IN PRICE PICTURE CAN BE EXPECTED IN REMAINDER OF YEAR.

HOWEVER, SECRETARIAT CONSIDERS 10 PERCENT OFFICIAL FORECAST TO BE ATTAINABLE ONLY IF (A) WAGE INCREASES ARE NOT EXCESSIVE (SECRETARIAT ASSUMES 15-16 PERCENT INCREASE IN AVERAGE NON-FARM EARNINGS); (B) IMPORT AND AGRICULTURAL PRICES REMAIN RELATIVELY STABLE; (C) THERE IS NO FURTHER DRACHMA DEPRECIATION.

5. CURRENT ACCOUNT: GREEK CURRENT ACCOUNT DEFICIT DECLINED TO \$1 BILLION IN 1975 COMPARED WITH \$1.2 BILLION DEFICIT IN 1974. PRIVATE CAPITAL INFLOWS COVERED ABOUT ONE HALF OF 1975 CURRENT ACCOUNT DEFICIT, AS FOREIGN EXCHANGE DEPOSITS IN GREEK BANKS AND REAL ESTATE PURCHASES BY GREEKS LIVING ABROAD AND SUPPLIERS CREDITS ALL ROSE CONSIDERABLY. THERE REMAINED CONTINUING NEED FOR PUBLIC BORROWING ON LARGE SCALE (\$600 MILLION INCLUDING DRAWING OF SDR137 MILLION ON IMF OIL FACILITY). SECRETARIAT FEELS THAT GREEK FORECAST OF \$1 BILLION 1976 CURRENT ACCOUNT DEFICIT IS SOMEWHAT OPTIMISTIC, AND PROJECTS 1976 TRADE DEFICIT OF \$3.3 BILLION AND CURRENT ACCOUNT DEFICIT OF \$1.2 BILLION. SECRETARIAT STRESSES MOUNTING BURDEN OF EXTERNAL DEBT AND IMPORTANCE OF GREEKS REACHING THEIR OBJECTIVE OF REDUCING CURRENT ACCOUNT DEFICIT IN MEDIUM TERM.

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6. MONETARY AND FISCAL POLICY: FISCAL POLICY WAS STRONGLY EXPANSIONARY IN 1975. PUBLIC CONSUMPTION ROSE SHARPLY; SPECIAL INVESTMENT RESERVE (SET ASIDE FOR USE IF NEED TO ENSURE RECOVERY) WAS FULLY EXPENDED AND GOVERNMENT FINANCING REQUIREMENT ROSE TO 3.5 PERCENT OF GNP. SECRETARIAT ASSUMES THAT INVESTMENT RESERVE (FOR WHICH FUNDS HAVE BEEN APPROPRIATED) WILL AGAIN BE SPENT IN 1976, AND FORECASTS INCREASE IN FISCAL STIMULUS WITH NET PUBLIC FINANCING REQUIREMENT REACHING 4.5 PERCENT OF 1976 GNP.

7. MONETARY POLICY IN 1975 WAS ALSO GEARED TO SUPPORT RECOVERY. ON AN AVERAGE ANNUAL BASIS, THE INCREASE IN M1 WAS 21 PERCENT, ABOUT 4 PERCENTAGE POINTS ABOVE INCREASE IN NOMINAL GNP. FOR CURRENT YEAR, GREEK AUTHORITIES FEEL THAT SOME SHIFT TOWARD MONETARY TIGHTNESS IS IN ORDER (TARGET IS 12 PERCENT INCREASE IN NOTES AND COINS IN CIRCULATION, WHICH INCREASED BY 15.7 PERCENT IN 1975), BUT POLICY ARRANGEMENTS WILL REMAIN FLEXIBLE AND WILL BE ADJUSTED ACCORDING TO NEEDS

OF ECONOMY AND DEVELOPMENT OF DEPOSITS. SECRETARIAT AGREES THAT LESS EXPANSIONARY MONETARY POLICY IS APPROPRIATE IN INTEREST OF FINANCIAL STABILITY, BUT COMMENTS THAT MONETARY RESTRAINT SHOULD BE OPERATED IN SUCH A WAY AS TO MINIMIZE IMPACT ON PRODUCTIVE INVESTMENT. (REFDOC NOT SPECIFIC AS TO HOW DIFFERENTIAL IMPACT WOULD BE PRODUCED.)

8. MEDIUM TERM: SECRETARIAT STRUCTURES DISCUSSION OF MEDIUM-TERM PROBLEMS AROUND OBJECTIVES SET OUT BY GREEKS IN NEW 5-YEAR PLAN (1976-80) CURRENTLY UNDER PREPARATION. MEDIUM-TERM OBJECTIVES ARE (A) 6 PERCENT ANNUAL INCREASE IN REAL GNP (VS 7-8 PERCENT AVERAGE OVER LAST 15 YEARS); (B) GROWTH OF FIXED INVESTMENT OF 10 PERCENT PER YEAR; (C) HALVING OF CURRENT ACCOUNT DEFICIT AS PERCENT OF GNP BY 1980 (CURRENT ACCOUNT DEFICIT WAS 5 PERCENT OF GNP IN 1975). SECRETARIAT COMMENTS THAT LOWERING OF GROWTH HORIZONS IS APPROPRIATE IN LIGHT OF CURRENT ACCOUNT AND INFLATION CONSTRAINTS. SECRETARIAT ALSO STRESSES IMPORTANCE OF SHIFTING INVESTMENT SPENDING LIMITED OFFICIAL USE
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AWAY FROM RESIDENTIAL CONSTRUCTION AND TOWARD EXPANSION OF PRODUCTIVE CAPACITY TO ABSORB INCREASING LABOR SUPPLY, TO ACCELERATE IMPORT SUBSTITUTION AND TO GENERATE NECESSARY INCREASE IN COMMODITY EXPORTS. CONCERNING LAST MENTIONED POINT, SECRETARIAT FORECASTS SLOWER INCREASE IN INVISIBLE RECEIPTS (REMITTANCES, SHIPPING RECEIPTS) THAN IN PAST, AND CONCLUDES THAT ACHIEVEMENT OF MEDIUM-TERM CURRENT ACCOUNT OBJECTIVE WILL BE IMPOSSIBLE WITHOUT MAJOR EFFORT TO EXPAND SHARE OF COMMODITIES IN CURRENT RECEIPTS.

9. BASED ON ANALYSIS REFDOC, SECRETARIAT SUGGESTS THAT EDRC CONCLUDE AS FOLLOWS:

(A) RECOVERY SHOULD CONTINUE AT MODERATE PACE IN 1976, BUT POSSIBILITY OF PRICE ACCELERATION AND CURRENT ACCOUNT DETERIORATION REMAIN AS MAJOR RISKS; THUS

(B) OVERALL DEMAND MANAGEMENT POLICY STANCE IN 1976 IS BROADLY APPROPRIATE (ESPECIALLY SINCE ELEMENTS OF FLEXIBILITY ARE INCLUDED), BUT EXPANSIONARY IMPACT OF FISCAL POLICY MAY BE AT LIMIT OF PRUDENCE;

(C) ACHIEVEMENT OF MEDIUM-TERM POLICY OBJECTIVES WILL REQUIRE POLICIES SUPPORTIVE OF NECESSARY SHIFT IN STRUCTURE OF INVESTMENT AND COMPOSITION OF EXPORTS;

(D) IMPLEMENTATION OF EFFECTIVE INCOMES POLICY WOULD
BE HELPFUL IN ACHIEVING BOTH SHORT- AND MEDIUM-
TERM GROWTH AND CURRENT ACCOUNT OBJECTIVES.

10. COMMENTS: (A) MISSION PLANS TO QUESTION GREEK REP
ON FINANCING OF 1976 CURRENT ACCOUNT DEFICIT AND ON TERMS
ON WHICH THEY EXPECT PRIVATE COMPONENTS OF SUCH FINANC-
ING TO BE AVAILABLE; (B) SECRETARIAT NOTES THAT INCREASE
IN BUSINESS FIXED INVESTMENT WILL BE NECESSARY TO SERVE
VARIOUS OBJECTIVES, ONE OF WHICH IS TO INCREASE PRODUC-
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TION OF COMMODITY EXPORTS AND OF IMPORT SUBSTITUTES.
INVESTMENTS OF THIS NATURE, HOWEVER, HAVE HIGH IMPORT
CONTENT. THUS, CURRENT ACCOUNT DEFICIT PROBLEM COULD
BECOME ACUTE BEFORE CORNER TOWARD IMPROVEMENT IS TURNED.
(C) MISSION PLANS TO QUESTION GREEKS ON PROSPECTS FOR
PRODUCTIVITY GROWTH IN 1976 AND IMPLICATIONS (ASSUMING
4 PERCENT GROWTH OF REAL GNP) FOR PRICE (AND/OR PROFIT)
PERFORMANCE, AND EMPLOYMENT. (D) GREEKS HAVE SET 1976
TARGET OF 12 PERCENT GROWTH OF NOTES AND COINS IN CIRCUL-
LATION. MISSION WOULD QUESTION GREEKS ON WHAT ACHIEVE-
MENT OF THIS TARGET IMPLIES FOR GROWTH OF OTHER MONETARY
AGGREGATES (I.E. M1), AND ON WHAT OPERATIONAL MECHANISMS
ARE EMPLOYED TO IMPLEMENT TARGET.
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